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In the Supreme Court of the United States

OCTOBER TERM, 1933

No. 349

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner.

v.

AMERICAN CHICLE COMPANY

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR THE PETITIONER

I

The respondent contends that this case is not controlled by this Court's decision in *United States* v. *Kirby Lumber Co.*, 284 U.S. 1, and bases its distinction between the two cases on the ground that in the *Kirby Lumber* case the taxpayer was a "borrower of money" while in the present case the taxpayer was a "purchaser of property." The respondent asserts (Br. 4) that in the *Kirby Lumber* case the taxpayer's bonds were issued "for money," and this same assertion is apparently the sole ground of the decision of the court below. (R. 29.)

We have already pointed out in our main brief (p. 10) that there is no basis for the assumption that the taxpayer in the *Kirby Lumber* case was a borrower of money and received cash in return for the bonds which it issued. The findings of the Court of Claims in that case do not disclose what payment was made for the bonds. They simply state that $12,126,800 of the bonds in question "were issued at par on July 16, 1923," and that the Kirby Lumber Co. received "the par value of the bonds issued, without incurring expense incident to the issue of the said bonds." (R. 12 in No. 26, October Term, 1931; 71 C.Cls. 290, 291–292.)

Moreover, the contention now made by the respondents and adopted by the court below was presented to this Court in the *Kirby Lumber* case. In stating the facts of the case in its brief in opposition to the Government's petition for certiorari, the taxpayer there asserted (p. 2) that the bonds in question "were not issued for cash, as stated by petitioner." And on p. 9 of the brief in opposition the same point was presented in more detail. The taxpayer there said:

> Counsel fully realizes that the Government would not intentionally mislead this Court for the purpose of securing the writ which is sought. However, a most serious distortion of facts is presented * * * because the Kirby Lumber Company DID NOT RECEIVE CASH for the bonds here involved.

> The bond issue simply resulted in a change in the capital structure of the corporation. Prior to the bond issue the balance sheet showed preferred stock as a liability, while after the bond issue the bonds were shown as the liability. There was no gain or profit, and no cash was received.

In answer to this argument in the brief in opposition the Government filed a reply brief in which it was contended (p. 1) that the Government's conclusion as to the facts was "a fair interpretation of the special findings of fact of the Court of Claims," but that, in any event (pp. 2–3), "whether the respondent received cash for the bonds is immaterial, since in some form the price received was 'the par value of the bonds issued.' "

On April 20, 1931, this Court granted the writ of certiorari sought by the Government. On May 8, 1931, the taxpayer filed a motion to remand the case to the Court of Claims "with instructions to make a finding with reference to the consideration received by the Kirby Lumber Company for the bonds issued by it in 1923." In this motion to remand it was again asserted (p. 2) that "No cash was received for the bonds," and the respondent contended that its motion should be granted "if the court believes the consideration received for the bonds is material." The Government opposed the motion to remand on the ground, among others, that "it is immaterial whether the respondent received cash or securities for the bonds."

When the Government's brief on the merits was filed, the taxpayer's contentions with respect to the facts were expressly recognized. The Government's brief did not assert that the bonds were issued for cash. It recited the taxpayer's statement as to the consideration received for the bonds, and then stated (Br. 2):

> The Government maintains that this does not alter the legal effect of the transaction so far as the present question is concerned. In any case, the Lumber Company received valuable consideration equal to the par value of the bonds. Upon issuing them, its assets and liabilities were increased in equal amounts.

In its opinion, this Court apparently accepted the Government's contention that the consideration received for the bonds was immaterial. In reciting the facts of the case, this Court said (284 U.S. 1, 2):

> In July, 1923, the plaintiff, the Kirby Lumber Company, issued its own bonds for $12,126,800 for which it received their par value.

It is to be noted that the Court did not say that the bonds were issued for cash. If it had regarded its decision as applicable only to bonds issued for cash, it seems probable that it would have said so. Moreover, the Government was the petitioner in the *Kirby Lumber* case, and consequently the burden was on it to present findings showing all facts necessary to establish its case; and since the findings

actually made by the Court of Claims did not disclose the consideration received for the bonds, they were necessarily read in the way least favorable to the Government's contentions.

From this recital of the record and briefs in the *Kirby Lumber* case, it seems to us to follow that this Court had squarely presented to it the question whether the nature of the consideration received for the bonds in a case such as this is a material factor, and that the decision of the Court must necessarily be taken as a decision that the nature of the consideration received is not material in the application of that case. We submit, therefore, that the *Kirby Lumber* case is direct authority for the Government's position here, and that the respondent's attempted distinction wholly fails.

II

The respondent also asserts that the principle that the purchase and retirement of an obligation incurred in connection with the purchase of property represents a payment on the purchase price of the property and is not a transaction giving rise to taxable gain "has heretofore been recognized and accepted by the petitioner." (Br. 8.) In support of this statement the respondent refers to a ruling of the Bureau of Internal Revenue issued in 1928 (I.T. 2406, VII–1 Cumulative Bulletin 68), and to the formal acquiescence of the Bureau in two decisions of the Board of Tax Appeals. The respond-

ent recognizes that the ruling relied on was issued before this Court's decision in the *Kirby Lumber* case, but states (Br. 9) that it "does not find that it has since been revoked or modified in any way."

The ruling referred to was adopted by the Bureau in conformity with a number of decisions of the Board of Tax Appeals which reached the opposite conclusion from that ultimately adopted by this Court. The ruling, and the acquiescenses in the Board's decisions, have not represented the Bureau's practice since this Court's decision in *United States* v. *Kirby Lumber Co.*, 284 U.S. 1, as is shown by the Bureau's position in the present case and in *Commissioner* v. *Coastwise Transp. Corporation*, 62 F. (2d) 332 (C.C.A. 1st). They were regarded as so plainly inconsistent with this Court's decision in the *Kirby Lumber* case that it was not necessary that they should be formally withdrawn. In order that there may be no question as to the Bureau's current practice, however, they have now been formally withdrawn and revoked. See Appendix A (*infra*, pp. 9–10).

III

The fallacy in the respondent's position becomes apparent, we submit, when the transaction by which it acquired the property of the Sen Sen Chiclet Company is viewed from the point of view of the seller. So far as the seller is concerned, it would seem to be obvious that the sale price of the

property was fixed when the property was sold, and could not thereafter be affected by subsequent transactions between the purchaser and other parties. It would seem to be equally obvious that the price received by the seller of the property and the cost to the purchaser, being two aspects of the same transaction, could not be different amounts.

This Court has already held that where property subject to a mortgage is sold and the purchaser assumes the mortgage, the amount of the mortgage must be included as a part of the purchase price in finding the seller's profit. *Burnet* v. *S. & L. Building Corp.*, 288 U.S. 406. To the same effect is *Lucas* v. *Schneider*, 47 F. (2d) 1006 (C.C.A. 6th), certiorari denied, 284 U.S. 622. The respondent makes no effort to distinguish these cases in its brief. Since it is settled that in such a case the amount of the mortgage is a part of the sale price of the property, it follows as a necessary consequence, we submit, that the amount of the mortgage is a part of the cost of the property to the purchaser. There would seem to be no escape from this conclusion where, as here, the purchaser's books are kept on the accrual basis. (R. 13.) The amount of the mortgage assumed became an accrued liability as soon as it was assumed. The discharge of that liability for less than its face amount could not alter the fact that the respondent had undertaken to pay a greater amount. The cost of the property was fixed when it was bought, and this

fact was reflected as an accrued liability on the respondent's books. That the discharge of that liability for less than its face amount increased the respondent's financial worth is obvious, and that it produced taxable income is, we submit, decided in *United States* v. *Kirby Lumber Co.*, 284 U.S. 1.

CONCLUSION

This case is controlled by the decision in the *Kirby Lumber* case. The decision of the court below is erroneous and should be reversed.

Respectfully submitted.

J. CRAWFORD BIGGS,
Solicitor General.

ERWIN N. GRISWOLD,
Special Assistant to the Attorney General.

FEBRUARY, 1934.

APPENDIX A

[SEAL] TREASURY DEPARTMENT,
BUREAU OF INTERNAL REVENUE,
Washington, January 31, 1934.

OFFICE OF THE GENERAL COUNSEL

Hon. J. CRAWFORD BIGGS,
Solicitor General, Department of Justice,
Washington, D.C.

In re: *United States* v. *American Chicle Company*, 65 Fed. (2d) 454.

MY DEAR MR. SOLICITOR GENERAL:

In connection with the above-entitled case, which is now pending before the Supreme Court of the United States, the taxpayer has cited in support of its position the acquiescenses of the Commissioner in the decisions of the Board of Tax Appeals in Des Moines Improvement Company, 7 B.T.A. 279, C.B. VII–1, 9, and American Seating Company, 14 B.T.A. 328, C.B. VIII–2, 2. I.T. 2406, C.B. VII–1, 68, which follows I.T. 2195, C.B. IV–2, 36, is also relied upon by the taxpayer. These acquiescences and rulings, all antedating the decision of the Supreme Court in United States v. Kirby Lumber Company, 284 U.S. 1, represented an effort by the Bureau to conform to the then current decisions of the Board and lower courts.

Since the decision of the Supreme Court of the United States in *United States* v. *Kirby Lumber Company*, supra, the principle enunciated in the

above-mentioned decisions of the Board of Tax Appeals and the Bureau has not been followed and has not represented the position of the Bureau. Formal revocation of the acquiescences and rulings was considered unnecessary in view of the Supreme Court's decision. However, to eliminate any misconception respecting the present position of the Bureau, acquiescences in the decisions of the Board of Tax Appeals in Des Moines Improvement Company and American Seating Company have been formally withdrawn, and I.T. 2195 and I.T. 2406 have been formally revoked.

Sincerely yours,

E. BARRETT PRETTYMAN,
General Counsel.

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